VZCZCXRO0828
RR RUEHCHI RUEHDT RUEHHM
DE RUEHJA #2759/01 2711015
ZNR UUUUU ZZH
R 281015Z SEP 07
FM AMEMBASSY JAKARTA
TO RUEHC/SECSTATE WASHDC 6501
INFO RUCPDOC/USDOC WASHDC 1507
RUEATRS/DEPT OF TREASURY WASHDC
RUEHZS/ASEAN COLLECTIVE
RUEHBJ/AMEMBASSY BEIJING 4358

UNCLAS SECTION 01 OF 02 JAKARTA 002759

SIPDIS

SIPDIS

DEPT FOR EAP/IET AND EB/TPP/ABT
DEPT PASS USTR BWEISEL; KATZ; CMILLER
USDOC FOR SBERLINGETTE/4430
USDOC FOR ITA/OTEXA MARIA D?ANDREA

E.O. 12958: N/A
TAGS: ECON KTEX ETRD EINV ID
SUBJECT: RESTRICTIONS ON CHINA BOOST TEXTILE EXPORTS

Ref: State 114799

¶1. (SBU) Summary: Indonesia?s textile and apparel sector registered 10% export growth over the last year despite slow-moving progress on national investment climate reforms. Much of the growth is accredited to U.S. safeguard measures against China as buyers look to Indonesia for geographic diversity. New investment in factories is restrained however by electricity shortages, labor rigidities and other investment climate issues. Meanwhile cheap imports from China continue to adversely impact the domestic market. End summary.

Benefiting from China + 1 Strategy

¶2. (U) Indonesia has all the ingredients to be one of the winners in the post-Multi Fiber Agreement world. It has a large, well-established, vertically integrated industry, including mills, garment factories and laundries. It has cheap and abundant labor, a large domestic market, and a proven capacity to produce quality mid to high-end textiles and garments for export. Buyers tell us that mid to high-end U.S. and European buyers are looking to Indonesia for geographic diversity to hedge against continuation of safeguards imposed on China (the ?China plus one? strategy).

Exports Still Going Strong

¶3. (U) Indonesia?s textile and apparel export performance has increased steadily over the last five years, despite a challenging investment climate. Textile and garment exports reached $9.5 billion in 2006, an increase of 10.5% from $8.6 billion 2005 year-on-year (YoY). Meanwhile employment in the sector remained stable. Industry contacts tell us the growth reflects the direct benefits of U.S. product specific safeguard quotas imposed on China. Indonesia?s textile exports to the US and EU increased by 27% and 3% respectively in 2006. According to API, exports to the U.S. and EU will remain robust as long as the safeguard measures imposed on China remain in effect.

Domestic Market Woes

¶4. (U) The domestic market for textiles and apparel has not fared as well as Indonesia?s export markets. This is particularly true for ready-made garments and fabric. The domestic market continues to suffer from the influx of less expensive Chinese products, both legal and illegal. Small- and medium-sized enterprises in the textile and apparel sectors have been affected most severely. Local producers complain they

simply cannot compete on price with low-end imports. Ministry of Trade data shows that, in spite of a 2002 Textile Decree forbidding the resale of textile imports locally, legal imports of textiles from China jumped from 340,549 to 675,300 kilograms between 2003 and 2004.

Factors Limiting Growth

¶5. (U) There is relatively little new investment in the textile and apparel sector due to slow progress on domestic investment climate issues, which continue to deter investment. Three issues that directly impact sector growth include: financing, infrastructure and labor.

-- (U) Financing: Manufacturers complain of a credit crunch caused by Bank Indonesia (BI) risk management guidelines for bank lending to sectors with higher than average rates of non-performing loans (NPLs). The textile and garment sectors fall into this category, with estimated NPLs of 8-9 percent in 2004. Manufacturers want banks to consider lending decisions on a company-by-company basis. With greater access to cheap capital, manufacturers say they could upgrade their textile and garment machines, which are 10 years old on average. New machinery in turn would improve quality and productivity and also enable Indonesia to maintain its competitive edge over China in mid- to high-end products.

-- (U) Infrastructure: Access to reliable and cost-effective energy for industrial production remains problematic. In October 2005, the state-owned electricity company PLN launched a ?dayamax plus? program restricting industrial production at peak-hours. Manufacturers complain of a subsequent 15 to 20 percent increase in electricity costs.

Manufacturers also see a lack of long-term investment in Indonesia's power sector and anticipate that ?rolling blackouts? across Java will become even more frequent and disruptive.

-- (SBU) Labor: The labor law provides on average nine months severance to dismissed workers, the highest rate in the region. Coupled with provisions against contract workers and outsourcing, the severance pay requirements encourage investors to establish factories for less than three years, close them down, and then reopen employing new workers. Manufacturers also seek more rational calculations for provincial minimum wage rates, with increases linked to inflation. Although not enthused with such reforms, some labor union leaders including Helmy Salim, the Secretary General for the Textile, Garment and Leather division of SPSI, said they were willing to cooperate with the government and industry to encourage greater investment.

2006 Data

¶6. (U) Both the Ministry of Trade and the Indonesian Textile Association (API) record textile data and employment on a yearly basis. However, the publication of their statistic is often delayed. API was unable to provide volume amounts for 2006.

-- Total Textile and Apparel Production:

	Volume (ton)	Value (US$ billion)
2005	4,103,000	14.1
2006	N/A	14.7

-- Textile and Apparel?s Share of Non-oil/Gas Indonesia Imports and Export: (in US$ billion)

	2005	Percent	2006	Percent
Export	8.6	12.9	9.5	11.9
Import	1.6	3.9	1.6	3.8

-- Exports in Textiles and Apparel to the U.S.

	Value (in US$ billion)
2005	3.08
2006	3.93

-- Total Manufacturing Employment:

2005	11,507,000 workers
2006	11,394,000 workers

-- Total Textile and Apparel Employment:

2005	1,841,520 workers
2006	1,839,869 workers

HEFFERN